BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 2002-6-G – ORDER NO. 2002-555A

AUGUST 15, 2002

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| IN RE: Annual Review of the Purchased Gas Adjustments (PGA) and Gas Purchasing Policies of South Carolina Pipeline Corporation. | ) ORDER ON PRUDENCE, PGA, AND RELATED MATTERS |

This matter comes before the Public Service Commission of South Carolina (the Commission) on its annual review of the Purchased Gas Adjustments (PGA) and Gas Purchasing Policies of South Carolina Pipeline Corporation (SCPC, Pipeline or the Company).

## I. INTRODUCTION

Commission Order No. 87-1122 provides that an annual review be conducted of SCPC's PGA and Gas Purchasing Policies. In this proceeding, the review period is January 2001 through March 2002. Petitions to Intervene were filed by the Consumer Advocate for the State of South Carolina (the Consumer Advocate), Chester, Lancaster, and York Natural Gas Authorities (the Authorities), the City of Orangeburg and Nucor Steel (Nucor).

A hearing was held in this matter on June 13, 2002, at 10:30 a.m. in the offices of the Commission, with the Honorable William Saunders, Chairman, presiding. SCPC was represented by Catherine D. Taylor, Esquire, and Mitchell Willoughby, Esquire. SCPC presented the testimony of Kevin Marsh, Paul V. Fant, and John S. Beier. The Consumer Advocate was represented by Elliott F. Elam, Jr., Esquire, and Hana Pokorna-Williamson, Esquire. The Authorities were represented by Paul Dillingham, Esquire, and John Gregg, Esquire. The City of

Orangeburg was represented by James M. Brailsford, III, Esquire. Nucor did not appear at the hearing. The Commission Staff (the Staff) was represented by F. David Butler, General Counsel. The Staff presented the testimony of Roy H. Barnette and Brent L. Sires.

## II. FINDINGS OF FACT AND CONCLUSIONS OF LAW

### A. GAS PURCHASING POLICIES AND PRACTICES

As an initial matter, we find that SCPC's purchasing policies and practices were prudent during the review period. SCPC witness Marsh testified in detail about SCPC's recent gas purchasing policies and practices, concluding they were prudent. Staff witness Sires reached the same conclusion.

During the review period, SCPC maintained a reliable and flexible portfolio of gas supply, storage, and capacity. (Testimony of Marsh at 4-6; Sires at 2.) SCPC continued to demonstrate that it places a high level of importance on securing reliable gas supplies and on making prudent decisions in purchasing its gas supplies. (Testimony of Sires at 3.) No supply problems were noted on the company's system during the review period. (Testimony of Sires at 3.) In addition, SCPC continues to exhibit its capabilities to secure gas supplies in a prudent manner and at reasonable costs. (Testimony of Sires at 3.) We therefore find that SCPC's gas purchasing policies and practices were prudent during the period of January 2001 through March 2002.

### B. ADHERENCE TO TARIFF

We also find that during the review period SCPC properly adhered to the tariff provisions relating to recovery of its gas costs. There was no dispute as to whether gas costs were properly recovered during the review period. SCPC witness Beier described the procedure the company followed for gas cost recovery, concluding that calculations were made in compliance with the approved tariff and Commission directives. (Testimony of Beier at 5-6.) Staff witness Barnette presented the Commission Staff's audit of the company's cost of gas, verifying that the cost of gas for the review period was properly accounted for. (Testimony of Barnette at 7-8.) Accordingly, we find that for the period of January 2001 through March, 2002 SCPC's gas costs were accurately stated, SCPC's gas cost recovery was calculated in compliance with Commission orders and the approved gas tariff, and the monthly cost of gas rates resulted in the precise recovery of actual gas costs incurred by the company.

C. INDUSTRIAL SALES PROGRAM-RIDER

Next, we find that the Industrial Sales Program Rider (ISP-R) continued to produce benefits for SCPC's firm customers and that the program should be continued. As SCPC witness Beier testified, the ISP-R allows SCPC to assign delivered gas costs to industrial customers at prices that are competitive with alternative fuel prices and enables SCPC to make interruptible sales that otherwise might not be made. (Testimony of Beier at 7-8.) Staff witness Sires confirmed that the ISP-R is needed for SCPC to effectively compete with alternate fuels in the industrial market. (Testimony of Sires at 8.) The ISP-R promotes more efficient use of SCPC's facilities, helps to recover a portion of SCPC's fixed costs through industrial sales, allows SCPC to exert purchasing power in interruptible gas markets so that natural gas is obtained at better terms and prices, and provides additional flexibility and reliability to SCPC's system. (Testimony of Beier at 7-8; Sires at 7-8.) For these reasons, the ISP-R should be continued without modification.

We deny the Consumer Advocate's Motion to modify the ISP-R to require the Company to assign gas to its interruptible customers with the highest cost with which the Company can still make the gas sale. According to the Consumer Advocate, nothing would change with the individual customer, in that the only change would be the cost of gas assigned to the customer. Pipeline argues that granting this Motion would increase the total cost of operating the system, and that the impact on Pipeline would be a reduction in margins and the inability to meet the Company's revenue requirement. Pipeline states that it would have to shift costs. However, Pipeline also alleges that there is not enough evidence in the record of this case to support this Motion, nor was Pipeline given any Notice that such a broad sweeping Motion would be presented at the time of the hearing. We frankly believe that we just simply do not have enough evidence in the record on this particular matter to properly consider the Consumer Advocate's Motion. We therefore deny it.

D. 20,000 DEKATHERMS PER DAY REQUIREMENT

By Commission order, SCPC is required to assign to the weighted average cost of gas (WACOG) 20,000 dekatherms of the least expensive daily delivered gas volume entering SCPC's system. (Testimony of Sires at 6-7.) During the period under review, this requirement caused SCPC to lose approximately $6,796,612 in approved margins and caused its sale-for-resale customers to lose approximately $368,745. (Testimony of Beier at 7.)

In this proceeding, no evidence was presented that would warrant modifying the 20,000 dekatherms per day requirement. Rather, Staff witness Sires testified that this level of lowest cost gas entering the WACOG was acceptable and that the Commission Staff recommended that it be continued. During the review period the impact to the cost of gas to customers whose gas purchases were made at the WACOG realized reductions in gas cost of $7,932,699. Of this amount SCE&G base rate customers realized gas cost reductions amounting to $5,989,708. (Testimony of Sires at 6.) No other witness or party took exception to Staff's recommendation. Accordingly, SCPC should continue to assign 20,000 dekatherms of the least expensive daily delivered gas volume to the WACOG.

E. PILOT HEDGING PROGRAM

We also find that SCPC's pilot hedging program was managed consistent with Commission orders during the period under review, has provided benefits to firm customers in the past, and should be continued at this time (see Beier and Sires testimony). The primary objective of the program is to reduce price volatility through the purchase of gas at the average market price over the long term. (Testimony of Beier at 8.) The Commission approved the pilot hedging program in 1995, initially allowing SCPC to hedge up to 30% of purchases for firm customers. The Commission allowed subsequent increases in volumes that may be hedged. Since 1997, SCPC has been allowed to hedge 75% of estimated purchases for firm customers. For the period under review, the result of the program was that the average hedging purchase price realized exceeded the average NYMEX market price, and resulted in gas hedges that were $26,156,743 greater than the average NYMEX market price. Since the inception of the program through March 31, 2002, the hedging program has resulted in gas hedges that are $23,520,341 greater than the average NYMEX market price. (Testimony of Beier at 11.)

Beier notes that the differentials are the natural result of pursuing the objectives of the program when markets deviated from historical patterns during the review period. While the Commission has found that the pilot hedging program was managed consistent with Commission orders during the period under review, we nevertheless are interested in encouraging additional dialogue and gaining further knowledge about the operations of the hedging program prospectively. Accordingly, the Staff is directed to schedule an undocketed, informal proceeding prior to the end of calendar year 2002, to review Pipeline's hedging program. The Commission, the Company, and all other interested persons will be provided an opportunity to discuss in a workshop, non-adversarial setting, the technical aspects and practices of the current hedging program. The objectives of the informal proceeding shall be to facilitate:

a. a discussion of the technical and economic merits of continuing the financial hedging program beyond 2003;

b. a review of the current statistical and financial data and model used by the Company to improve the understanding of the Commission and other interested persons regarding the hedging program;

c. establishment of specific criteria used to determine when to hedge less than the 75% currently allowed maximum under the prior Commission Orders;

d. a discussion of potential modifications and improvements to the current hedging program to avoid a reoccurrence of the extreme volatility and price increases to the average cost of gas experienced during the review period in this Docket.

The informal hearing in this matter shall be transcribed. We hereby waive that portion of our Regulation 103-820 which would prohibit transcription of the informal proceeding. We believe that the waiver is in the public interest, in that a record of our informal proceeding would be a useful tool for further analysis of the Company's hedging program prospectively.

## F. MISCELLANEOUS MATTERS

We would note that our Commission Order No. 2001-496 instructed the Commission Staff and SCPC to enter into non-binding informal discussions related to the concern raised by Commissioner Atkins during the 2001 hearing regarding SCPC's lack of a strategy or specific methodology to determine how best to manage storage capacity. The purpose of these meetings was to consult on the advisability of the Company establishing or adopting a storage management plan. Whereas, the discussions appeared to have taken place, as evidenced by the testimony of Company witness Fant and Staff witness Sires, we believe that further action is necessary on the matter of storage.

Accordingly, within three (3) months from the date of issue of this Order, the Company shall conduct a study and provide the Commission a written report on the advisability of establishing a gas storage management and operation plan. The study shall include the following items:

a. A compilation and analysis of available empirical data from the Company, other gas utilities and/or industries, as well as a focused literature review of published research, on the potential economic, reliability, and operational benefits of utilizing a gas storage management model.

b. An evaluation of various simulation and optimization models to determine the "best" modeling alternative for the Company. The evaluation shall include a review of both "off the shelf" and/or proprietary linear, dynamic, networking and other non-linear search techniques. Consideration shall also be given to the applicability of any coupled statistical techniques, to the simulation or optimization model, to describe uncertainty within gas markets.

c. An estimate of the costs to purchase any software and any recurring costs such as license fees, consultant fees, data collection or personnel costs to maintain the storage management model.

d. Other such information related to this matter which the Company considers of interest, relevance or value.

An additional miscellaneous matter is the review period itself. The Company had proposed permanent modification of said period to a twelve-month period from April 1 – March 31 for each review period, rather than the traditional twelve month calendar month period seen in prior Pipeline PGA Dockets. We decline to order said modification. We believe that the calendar year review period has been satisfactory in the past, and believe that said review period should continue. The next docket shall review the period April 2002 through December 2002, however, after that, the review period shall return to the calendar year.

IT IS THEREFORE ORDERED THAT:

1. SCPC's gas purchasing policies and practices during the period January 2001 through March 2002 are found to be prudent.

2. SCPC is found to have properly adhered to the gas cost recovery provisions of its gas tariff during the period January 2001 through March 2002.

3. The requirement that SCPC assign to the WACOG 20,000 dekatherms of the least expensive daily delivered gas volume shall be continued.

4. The ISP-R shall be continued without modification. The Consumer Advocate's Motion is denied.

5. SCPC is found to have managed the pilot hedging program during the period under review consistent with Commission orders, and the hedging program shall be continued at 75% of estimated gas purchases for firm customers at the present time. An informal proceeding shall be established for the purpose of discussing the pilot hedging program as indicated and delineated above.

6. The Company shall, within three months from the date of issue of this Order, conduct a study and provide this Commission a written report on the advisability of establishing a gas storage management and operation plan, with the features as delineated above.

7. The calendar year review period shall remain in place. The next review shall be for the period of April 2002 through December 2002. Subsequently, the calendar year shall be the review period.

8. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Chairman

ATTEST:

Executive Director

(SEAL)